

REPORT BY THE STATE AUDITOR OF CALIFORNIA

**STATUS REPORT ON THE ORANGE COUNTY
TREASURER'S OFFICE**



CALIFORNIA STATE AUDITOR

BUREAU OF STATE AUDITS

KURT R. SJOBERG
State Auditor

MARIANNE P. EVASHENK
Chief Deputy State Auditor

January 18, 1995

94026.1

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

This letter represents the status of our audit of Orange County's (county) investment funds. After meeting with county officials, we started our work on December 13, 1994.

Initially, we focused our effort on three areas:

1. Reconciling and verifying the assets held by the Orange County Treasurer on behalf of various county agencies and outside investors;
2. Assessing short-term cash demands of the county's operational needs and the cash needed to pay interest on the county's outstanding bonds; and
3. Reviewing the expenditure, income, and trading activity from the investment fund since June 30, 1994.

Since that time, at the request of the Joint Legislative Audit Committee, we have expanded the scope of our audit to include a review of the county's contracts with financial advisors and a determination of the fees paid to Merrill Lynch by the county.

We have completed our work on Item 1. In the following section, we describe our work on this item.

On December 6, 1994, county officials filed bankruptcy on behalf of the county and the other participants in the county's investment pool. On December 12, 1994, Salomon Brothers, who had been retained by the county to restructure the investment portfolio, estimated that the portfolio had sustained a \$2.02 billion loss. Since December 12, 1994, a more accurate picture of

the loss has evolved as the actual value of the investments was determined through sales and as better information became available. In providing the better information, the county was assisted by Arthur Andersen & Co., an accounting and consulting firm.

We worked with Salomon Brothers and Arthur Andersen & Co. staff to determine a current revision to the loss that was estimated in December. In determining the revision, we reviewed the assets of the investment portfolio as well as the amounts owed to the various participants. We relied on the sales information as provided by Salomon Brothers. Based on the procedures we performed, we believe that the revised loss as shown in the following schedule is materially accurate.

Orange County Investment Portfolio
Original and Revised Estimates of Loss in Value
(Dollars in Billions)

	Original Estimate as of 12/12/94^a	Revised Estimate as of 1/17/95^b
Amount contributed by fund investors	\$7.42	\$7.57
Market value of securities held	5.03	5.16
Cash and equivalents	0.23	0.54
Value of excess collateral held by dealers	0.04	0.00
Value of excess collateral collected or due from liquidations by dealers	0.10	0.18
Loss	\$2.02	\$1.69

a Original estimate computed by Salomon Brothers.

b The estimate does not include \$53 million of specific investments that are not held by Bank of America. Since the amount was also not included in the amount contributed, there is no effect on the loss.

The schedule presents the value of securities based on sales of the portfolio through January 17, 1995. The county's investment portfolio loss, based on current information, is \$1.69 billion, or \$330 million lower than originally estimated in December 1994. This decrease is primarily a result of the better information that is now available regarding the assets of the portfolio and the amount owed to participants. Additionally, a portion of the decrease results from sales activity

Letter Report 94026

January 18, 1995

Page 3

that was better than anticipated. The loss could further change based on future sales activity although such changes are not expected to be significant, as most of the portfolio has been sold.

We continue to work on the remaining items and plan to issue an interim report on Item 2 within the next two weeks. Our final report, which we plan to issue in March, will cover the remaining items.

We conducted this review under the authority vested in the state auditor by Section 8543 et seq. of the California Government Code and according to generally accepted governmental auditing standards. We limited our review to those areas discussed in this letter.

Sincerely,

A handwritten signature in cursive script, reading "Kurt R. Sjoberg". The signature is written in dark ink and is positioned above the printed name and title.

KURT R. SJOBERG

State Auditor